

Wealthspire 2025 Q4 Review

Policy Pivots Reinvigorate Diversification

By the Wealthspire Investment Team

Entering the new year, investors find themselves reflecting on the last twelve months, assessing what took place and where we go from here. With the multi-pronged support of monetary and fiscal policy, the U.S. economy continued to shine, leading to continued profitability for corporate America and strength across risk assets. In this letter, we also talk about the Fed policy pivot and how diversified portfolios worked in a year when so much focus was on artificial intelligence (AI).

Mid-Cycle Easing & the Pursuit of a Soft Landing: 1994–95 vs. 2025

One question that entered conversations recently surrounds the idea that “if the economy is cooling, why doesn’t it feel like a downturn?” The simplest answer is that the Federal Reserve helped guide the economy towards a soft landing, whereby inflation decelerated and growth slowed without tipping into recession. This is a rare outcome, though not unprecedented, and one that harkens back to the mid-1990s.

In 1994, the Federal Reserve executed one of the fastest tightening campaigns of that era, lifting the policy rate from roughly 3% to 6% by early 1995, tapping the economic brakes to slow the economy before shifting to an easing cycle. On July 6, 1995, the Fed trimmed rates by a modest 0.25%, noting that inflationary pressures had “receded enough” to warrant a small adjustment. The next day, headlines summed up the intent plainly: the Fed cut “to spur the economy” amid “mounting signs of a weakening” backdrop. The Chicago Fed labeled it a bumpy runway, but ultimately not a recession, and later retrospectives highlighted 1994–95 as the rare hiking cycle that didn’t end in a downturn. With its monetary policy pivot, the Fed gave just enough support for the economy to continue expanding until the end of the decade when the bursting of the tech bubble finally ended one of the longest expansions on record.

2025 rhymes with that time as inflation cooled meaningfully through autumn, seen in the Consumer Price Index (CPI) which finally started to drift below 3% year-over-year. The second leg of the Fed’s policy mandate stool is the job market, and though it softened, it has yet to crack, with unemployment ending December at 4.4%. The Fed delivered three interest rate cuts into year-end after stresses in the labor market grew substantial enough to overcome worries about inflation. None of this means the runway is perfectly smooth. Data quirks (like the shutdown-delayed CPI report) muddied the monthly picture, and tariff adjustments can still push inflation higher for category-level prices. But the bigger story remains constructive: inflation is moving down, employment is cooler but steady, and policy shifted toward preserving growth rather than restricting. Like the mid-1990s, today’s economy is trying to fly slower without stalling. That’s the essence of a soft landing, and it’s the backdrop we expect investors to navigate into 2026.

Reports of My Demise Are Greatly Exaggerated

In a year filled with twists, diversified portfolios returned to favor with differing engines of return kicking into gear at important points throughout the year. Investors faced new tariff policies that reshaped supply chains, navigated data gaps from the government shutdown, and digested softening labor conditions and policy uncertainty. It was a classic wall of worry that gave investors plenty to fear and little to cheer. Yet alongside those fears, income on bonds came back in vogue, international stocks led for the first time in years, and pockets of real assets found footing alongside the buildup in artificial intelligence infrastructure. The result was that diversified portfolios worked exactly when investor questions began to arise about whether it was time to move on to something new. Over short windows, markets often follow sentiment with headlines

and momentum pushing prices higher and lower without complete rationality. Over the long run, returns tend to follow **earnings, cash flows, and income**, the proverbial building blocks of a diversified portfolio.

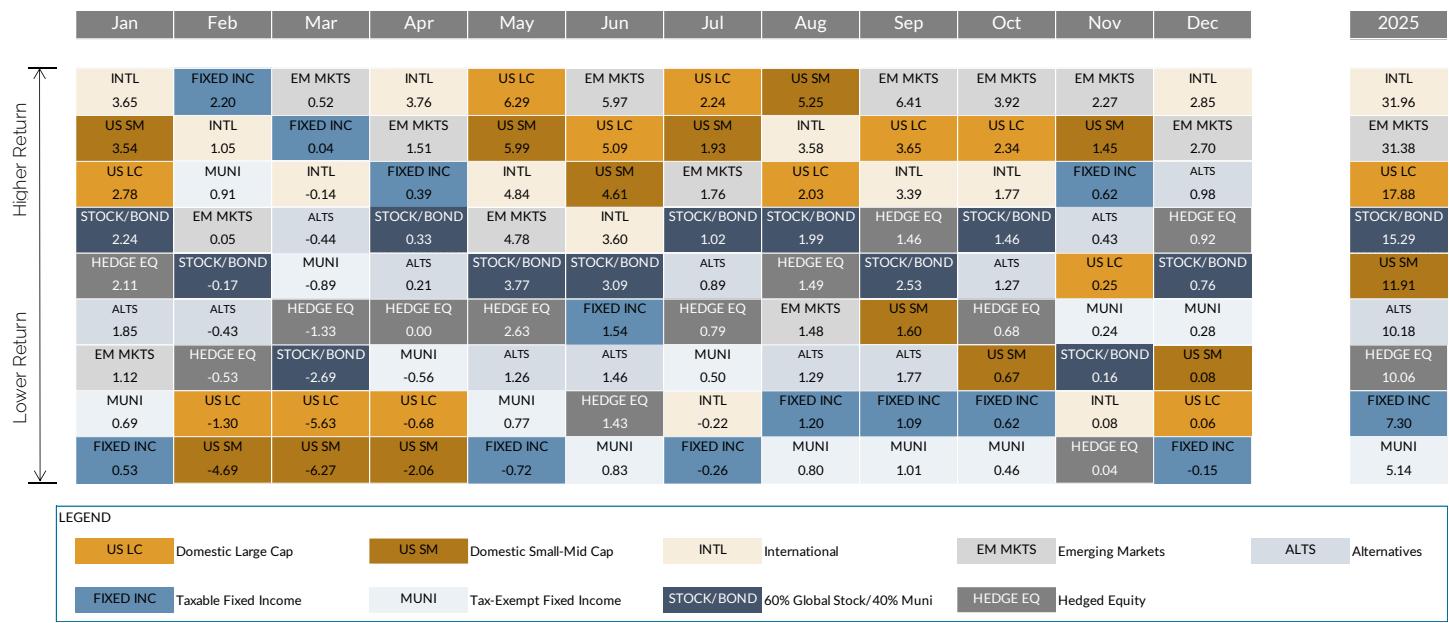
Diversification tailwinds came down to one obvious and important reason – starting points matter. We discussed previously that all-time highs beget new all-time highs in short bursts, but over the long haul, price matters and whether in fixed income or stocks, if your starting point is favorable, it translates to better outcomes. We entered 2025 with fixed income yields at levels not seen for much of the past fifteen years. The Bloomberg Aggregate Bond Index started the year with a yield to worst of 4.90%. Once we learned inflation trends were cooling and the Fed would likely cut interest rates, it acted as a tailwind for bonds, allowing most segments of fixed income markets to rise for the year. Despite the resulting decline in rates, yields remain constructive, which should allow high quality bonds to restore the portfolio ballast status many investors missed in 2022, while letting coupons compound quietly in the background.

Leadership also broadened beyond the U.S., a rotation investors thought may never happen. International stocks gained more than 30% in 2025, with strength across developed and emerging markets that was aided by cheaper starting valuations and currency dynamics that rewarded going global. We talked previously about lower valuations and better fundamentals as a key consideration for incorporating non-U.S. stocks into portfolios. That continues to be true when looking at both developed and emerging market stocks. Valuations on a price/earnings or price/cash flow basis are comparable to mid and small-cap U.S. stocks, though profit margins and return on equity now surpass the same cohort. The point of global diversification is never about abandoning U.S. exposure, but rather balancing risk factors and allowing regional cycles to contribute when the U.S. takes a breather.

The simple narrative for last year is this: diversification worked in 2025 because no single driver dominated despite headlines that continually broadcast the trends in AI. Inflation moved down (despite shutdown related data noise), policy leaned toward accommodation rather than restriction, and global leadership broadened enough that portfolios didn't have to rely on one style, one sector, or one country to carry the year.

We are sticking with the principles that made 2025 a constructive year for diversified portfolios, which are to stay balanced, incorporate a global approach to equity investing, emphasize cash flows, and manage liquidity with intent. The advantage moves beyond the mathematical and into the behavioral, blending the proverbial science with the art. Diversification offers more ways to be right and fewer reasons to abandon a sound plan when the next headline arrives. In the year ahead, we are bound to see headlines referencing geopolitical risk, midterm elections, and expensive equity markets. Creating durability in the portfolio provides comfort that we can navigate through the headlines over longer time frames that align with the goals and needs of our clients.

Markets



Source: Morningstar and Bloomberg Finance L.P. (data as of 12/31/2025)

- Stock markets ended on a high note, with the S&P 500 index up 2.7% for the quarter and 17.9% for the year. Domestically, large cap stocks were the top performer. Earnings growth of the largest companies, particularly those with AI links, outpaced that of smaller firms. International markets moved back to the top spot, with international developed up 4.9% and emerging market stocks up 4.7%. Those markets ended the year up more than 30%.
- Bond markets were up in the fourth quarter to close out a third consecutive positive year. The Federal Reserve cut rates further, finishing 2025 with an overnight policy rate of 3.50 - 3.75%. The Fed cited the slower pace of labor markets as a concern, while reminding everyone that they will remain vigilant about potential inflation pressures. The 10-year closed the year at 4.17% down from 4.60% at the end of 2024. Interest rates fell mid-September and then bounced around into year-end. The Bloomberg US Aggregate Bond Index (proxy for investment grade taxable bonds) finished the year up more than 7%, outpacing Municipal bonds which were up closer to 5%.
- Although there were concerns about a pickup in defaults and potential for market softening during the year, credit markets did not budge as investment grade corporate bonds returned 7.3% and high yield bonds gained 8.6%. Interest rates falling was a primary tailwind, but economic resilience (and therefore tighter spreads) also played a role. Returns are likely to be slower in credit markets with rates already lower and spreads tight, suggesting that investors should manage expectations going forward.
- Commodity markets offered a mixed picture in 2025 with energy prices lower, though metal prices higher. Gold and silver prices soared throughout the year alongside fiscal headlines, a weaker Dollar, and currency debasement concerns. Meanwhile, energy prices sank given higher output production from OPEC and other countries.

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